# No. 21,003

IN THE

# United States Court of Appeals

## For the Ninth Circuit

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PASADENA INVESTMENT COMPANY and WILLIAM J. CLARK,

*Appellants,*

vs.

MARGUERITE J. WEAVER,

*Appellee.*

## APPELLEE'S BRIEF

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### STATEMENT OF PLEADINGS AND FACTS DISCLOSING JURISDICTION

On June 22, 1965, appellee Marguerite J. Weaver filed her petition for an arrangement under Chapter XI of the Bankruptcy Act. On August 2, 1965, Marguerite J. Weaver, as debtor in possession, filed a Petition to Determine Validity, Nature, Extent, Priority and Amount of Claims of Lien on debtor's real property against respondents Pasadena Investment Company, William J. Clark and Title Insurance and Trust Company. (T. p. 13.)[1] A three day trial was

[1](References used in this brief are "T." for the Transcript of Record certified by the Clerk of the United States Court of Appeals for the Ninth Circuit and "R.T." for the Reporter's Transcript of testimony taken at the trial.)

held before Honorable Donald R. Franson, Referee In Bankruptcy and the Findings of Fact, Conclusions of Law and Order of the Bankruptcy Court were entered on November 15, 1965 (T. p. 57), holding that a promissory note and deed of trust executed by appellee and her late husband on August 28, 1963 were void for fraud, mistake and failure of consideration.

On November 19, 1965, appellants filed a Petition for Review (T. p. 69) pursuant to Bankruptcy Act §39c (11 USCA 67c). On March 29, 1966 the Honorable M. D. Crocker, United States District Judge, filed his Order which affirmed the Referee's order of November 15, 1965 (T. p. 162), pursuant to the jurisdiction of the United States District Court to consider findings and orders certified by referees and to confirm, modify or reverse such findings and orders under Bankruptcy Act Section 2a (10), (11 USCA 11) and General Order 47 (General Orders In Bankruptcy adopted by the Supreme Court of the United States).

Appellants filed their Notice of Appeal on April 13, 1966 (T. p. 151) and jurisdiction is conferred upon this court by Bankruptcy Act Section 24a (11 USCA 47a).

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## STATEMENT OF THE CASE

The Findings of Fact (T. p. 57) contain a concise summary of the facts of the case. The appeal raises only two issues: one, whether the Bankruptcy Court had summary jurisdiction to make its order voiding the

debtor's promissory note secured by deed of trust on the debtor's real property on grounds of fraud, mistake and failure of consideration; and two, whether there is evidence to support the Bankruptcy Court's finding that the debtor is not estopped to assert the grounds of fraud, mistake and failure of consideration against appellant William J. Clark who purchased the note and trust deed after the note was past due.

Since the estoppel issue is the only issue on the merits in this appeal, the facts relating to it are fully set forth in paragraph II of the Argument in this brief, where that issue is treated.

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## ARGUMENT

### I.

### THE BANKRUPTCY COURT HAD JURISDICTION TO RULE UPON THE VALIDITY OF THE PROMISSORY NOTE AND DEED OF TRUST.

#### A. The Bankruptcy Court Had Jurisdiction by the Consent of Both of the Appellants.

Both Pasadena Investment Company and William J. Clark, respondents to debtor's petition to determine the validity, nature, extent, priority and amount of their claims of lien against debtor's 55 acre ranch, consented to jurisdiction by filing their answers in the Bankruptcy Court. The applicable part of Section 2a(7) of the Bankruptcy Act (11 USCA 11) provides as follows:

> ". . . where in a controversy arising in a proceeding under this Act an adverse party does not interpose objection to the summary jurisdiction of the court of bankruptcy, by answer or motion filed before the expiration of the time prescribed by law or rule of court or fixed or extended by order of court for the filing of an answer to the petition, motion or other pleading to which he is adverse, he shall be deemed to have consented to such jurisdiction;"

The answer of Appellant, Pasadena Investment Company, contains absolutely no objection to the summary jurisdiction of the Bankruptcy Court to proceed to hear the petition. In fact, it prays for affirmative relief:

> "Wherefore your respondent prays this court make an appropriate order establishing the validity of the promissory note and deed of trust and authorizing the holder of the promissory note and deed of trust do (sic) all things necessary and proper in the foreclosure of said deed of trust and sale of the real property pursuant to and in accordance with the terms of said deed of trust." (T. p. 19.)

Thus, Pasadena Investment Company invoked the Bankruptcy Court's jurisdiction to determine that the deed of trust was valid, and consented to the Bankruptcy Court's jurisdiction. (Collier on Bankruptcy, 14th ed., Vol. 2, paragraph 23.08 (5); *In re Engineers Oil Properties Corp.* (S.D. N.Y. 1947) 72 F. Supp. 989.

The answer of the appellant, William J. Clark, does not object to the summary jurisdiction of the Court, but alleges "that the Court has no jurisdiction under Section 4 of the Bankruptcy Act over thirty-eight (38) of the fifty-four (54) acres shown in exhibit 'A' of debtor's petition . . .". Appellant Clark then invoked the jurisdiction of the Bankruptcy Court by praying for affirmative relief:

> "Wherefore, your respondent prays this Court make an appropriate order establishing the validity of the promissory note and deed of trust and authorizing the Title Insurance and Trust Company, as Trustee, holder of the promissory note and deed of trust, to do all things necessary and proper in the foreclosure of said deed of trust and sale of the real property, pursuant to and in accordance with the terms of the said deed of trust; and that the rent money collected since the filing of the Bankruptcy be ordered to be returned to be held by the Court appointed Trustee, as part of the security for respondent beneficiary under the terms of the Trust." (T. p. 29.)

At no time did either appellant argue that the Bankruptcy Court had no jurisdiction. An examination of the transcript will show that the oral arguments of both respondents at the time of trial were based solely upon the proposition that the Bankruptcy Court had no jurisdiction over *part* of the ranch acreage. Pasadena and Clark on the first day of trial argued that thirty-eight (38) acres of the ranch plus one-half of the remaining acreage was the separate

property of the debtor's deceased husband, Charles L. Weaver, Sr. and that this property was under the sole jurisdiction of the Probate Court in Tulare County. (R.T. pp. 1-18.)

> "The Referee: Do you contend that this court doesn't have jurisdiction to determine the validity of this deed of trust insofar as Marguerite J. Weaver's interest is concerned?
>
> Mr. Davidson: No. I do not contend as far as the 6 acres is concerned . . .
>
> The Referee: We're in agreement on that point.
>
> Mr. Davidson: Right. We're in agreement on that point. . . ." (R.T. p. 9; see also R.T. p. 66.)

Appellant's only real argument about jurisdiction was that the Bankruptcy Court had no jurisdiction over a part of Mrs. Weaver's ranch. Since both appellants invoked the aid of the Bankruptcy Court in declaring the subject Promissory Note and deed of trust valid, there should be no question that the Bankruptcy Court had summary jurisdiction by their consent.

**B. The Bankruptcy Court Had Summary Jurisdiction to Determine the Validity of the Deed of Trust Because It Affected the Debtor's Title and Ownership of Her Real Property.**

**1. Mrs. Weaver Owned the Ranch and Her Title Was Not in Dispute.**

The ranch belonged to Mr. and Mrs. Weaver, Sr. (R.T. pp. 23-26) and had been leased since 1958 when Mr. Weaver, Sr. retired (R.T. p. 31, R.T. p. 58). The ranch is located within the jurisdiction of the Bankruptcy Court a few miles outside the City of Tulare,

California. (R.T. p. 22, R.T. p. 59.) The Weaver Seniors did not live on the ranch but lived in the City of Tulare. (R.T. p. 19, R.T. p. 53.) The ranch was unencumbered when Mr. and Mrs. Weaver, Sr. signed the promissory note for $51,000.00 secured by a deed of trust on their ranch on August 28, 1963. (Debtor's Exhibits 8 and 9; R.T. p. 22.) Charles L. Weaver, Sr. was killed on August 18, 1964 (R.T. p. 19) leaving a will with his wife, Marguerite J. Weaver, the debtor herein, as sole beneficiary and executrix (Debtor's Exhibit 1). Mrs. Weaver filed her petition under Chapter XI on June 22, 1965. At that time the property was physically in the possession of a subtenant. Neither respondent Clark nor respondent Pasadena was in possession. (R.T. pp. 56-58.) On July 7, 1965, the will was admitted to probate in Tulare County and Mrs. Weaver was appointed executrix of the will of Charles L. Weaver, Sr. (Debtor's Exhibits 2 and 3.)

Mrs. Weaver had title to the ranch from the date of her husband's death on August 18, 1964. The general rule is that real property vests instantly at the death of the testator. Collier on *Bankruptcy,* 14th ed., Vol. 4, p. 1232, §70.27; Atkinson on *Wills* (1937) pages 528-529; California Probate Code §300. In California, when a person dies, the title to his property, real and personal, passes to the person to whom it is devised or bequeathed by his last will subject only to the possession of the executor and to the control of the Superior Court for the purposes of administration. (Probate Code §300.) In other words, title

does not come from the decree of distribution, which merely declares the title that came from the will or through the death of the decedent. (See *U.S. Fidelity, etc. Co. v. Mathews,* 207 Cal. 556, 279 P. 655; *Murphy v. Crouse,* 135 Cal. 14, 66 P. 871; *Reed v. Hayward,* 23 Cal. 2d 336 at 342, 73 P. 2d 247 at 252.)

**2. The Bankruptcy Court Had Exclusive Summary Jurisdiction Based Upon Mrs. Weaver's Undisputed Title to the Ranch.**

Since many of the cases cited in the following discussion arise in straight bankruptcy proceedings it is helpful to keep in mind that the debtor in possession under a Ch. XI arrangement proceeding has the same powers as a trustee in bankruptcy. As stated in Section 342 of Ch. XI of the Bankruptcy Act ". . . the debtor shall continue in possession of his property and shall have all the title and exercise all the powers of a trustee appointed under this Act . . ." Also, Section 302 makes the provisions of Chapters I through VII of the Bankruptcy Act applicable to Ch. XI proceedings whenever they are not inconsistent. (11 USCA 742 and 702.)

Appellants challenge the jurisdiction of the Bankruptcy Court because Mrs. Weaver's ranch was leased and she was not in physical possession of it. (Argument, Section I, Appellants' Opening Brief, pp. 15-18.) The point is attempted to be based upon the well recognized rule that where an adverse claimant is in possession of property, the Bankruptcy Court has no summary jurisdiction to determine the title or rights in the property held by the adverse claimant. In our

case Mrs. Weaver is the owner of the real property, a subtenant who has no dispute with the debtor is in physical possession of the real property, but the issue is between Mrs. Weaver and the appellants who are not in physical possession of the real property.

Section 311 of the Bankruptcy Act states that the Bankruptcy Court shall have exclusive jurisdiction over the debtor and his property.

> "Where not inconsistent with the provisions of this Chapter, the court in which the petition is filed shall, for purposes of this Chapter, have exclusive jurisdiction over the debtor and his property, wherever located." (Bankruptcy Act, Sec. 311, 11 USCA 711.)

This Court has stated that Section 311 confers exclusive summary jurisdiction over property not in the debtor's possession where the debtor's title is not in dispute:

> "Section 311 confers exclusive summary jurisdiction to determine controversies to property owned by the debtor, or in the actual or constructive possession of the debtor or the bankruptcy court. *Slenderella Systems of Berkeley, Inc. v. Pacific Tel & Tel Co.* (2 Cir. 1961) 286 F 2d 488, 490, see 8 Collier on Bankruptcy (14th Ed 1963) ¶ 3.02. This includes property not in the possession of the debtor, where the debtor's title is not in dispute. See 8 Collier, Supra, at 181-182."
>
> *Loyd v. Stewart & Nuss, Inc.,* (C.A. 9th 1964) 327 F. 2d 642 at 645.

Since Mrs. Weaver's title to the ranch is not in dispute, the Bankruptcy Court has exclusive sum-

mary jurisdiction based upon Section 311 of the Bankruptcy Act.

**3. Mrs. Weaver as a Lessor Owns the Underlying Title to Her Leased Real Property and It Is by Law in the Constructive Possession of the Bankruptcy Court and Subject to Its Summary Jurisdiction.**

The law of real property generally and in California specifically, defines as a "reversion" that which the lessor has left after he has leased real property for a term of years to a tenant. In California the lessor's reversion is defined as follows:

> "A reversion is the residue of an estate left by operation of law in the grantor or his successors, or in the successors of a testator, commencing in possession on the determination of a particular estate granted or devised." (California Civil Code Section 768; see Ogden's *California Real Property Law,* Sections 2.10 and 2.11.)

A lessor, as owner of real property, may sell the land during an unexpired leasehold term, in which event the vendee becomes the landlord by operation of law and the tenant becomes a tenant of the vendee of the reversion. (*Upton v. Toth,* 36 C.A. 2d 679, 98 P. 2d 515.)

Thus in our case Mrs. Weaver was the owner of the ranch which she had leased out. Her property rights were the right to receive rent under the lease and her reversionary interest in the land. The case of *Benton v. Calloway,* 165 F. 2d 877 (5th Cir. 1948) affirmed by the United States Supreme Court in 336 U.S. 132, 69 S. Ct. 435, 93 L. Ed. 553, is directly in point except that it must be kept in mind that it was

the tenant who was the debtor in that corporate reorganization proceeding. The Court in the *Calloway* case states that because the lessee in actual possession of the tangible property leased by it is the debtor, the Bankruptcy Court has summary jurisdiction over the leased property but does not have summary jurisdiction over the reversion in the leased premises because the lessor is not in bankruptcy. On the other hand, the Court states that if the lessor were in bankruptcy, then the Court would have jurisdiction in rem over the reversion but not over the tenant's leasehold, and the reversion being intangible property, the ownership of it in the lessor carries with it the legal consequences of possession, giving the Bankruptcy Court summary jurisdiction.

> "The debtor was in actual possession of the tangible property leased by it, but it held the same as lessee, not as owner in fee. The granting of a lease always supposes the grantor reserves to himself a reversion in the leased premises. A leasehold estate is personal property which becomes subject to the exclusive jurisdiction of the bankruptcy court upon the filing of a petition by the debtor under said section 77; but the lessor's title in fee, out of which the leasehold was carved, was not an asset of the debtor, and no claim of title thereto or lien thereon is made by the debtor or its trustee.
>
> The jurisdiction of the federal district courts sitting in bankruptcy is limited to matters conferred by statute expressly or impliedly. Such jurisdiction is paramount and exclusive in the administration of the bankrupt's estate. The

basis of the court's exclusive jurisdiction in rem is its actual or constructive possession of the debtor's property. It is not limited to the administration of property that belonged to the debtor without question, but extends to the determination of all questions of title or liens affecting the debtor's estate. It is not exclusive as to the right or title of a party not in bankruptcy to property not legally or equitably owned or claimed by the debtor. . . ." (Page 880.)

. . .

"It is well settled that the bankruptcy court has no summary or exclusive jurisdiction in rem of tangible property adversely held by a third party under a bona fide claim of ownership. The same is true of intangible property, except that ownership of the latter carries with it the legal consequences of possession. *In the case of a reversion the law attributes to ownership the jurisdictional consequences of possession.* To illustrate, let us suppose that South-Western (the lessor) were the debtor here, and that Central (the tenant) were a solvent corporation holding under its lease. *The bankruptcy court would have jurisdiction in rem, of the reversion, but not of the leasehold.*" (Page 882, emphasis added; material in parenthesis added.)

The same rules are laid down in *Texas and N.O.R. Co. v. Phillips* (5th Cir.), 211 F. 2d 419; certiorari denied 348 U.S. 913, 75 S. Ct. 293, 99 L. Ed. 716.

The case at bar is an illustration of the general rule that where the character of the property is such that it is not capable of tangible or actual physical

possession the law deems such property to be in the constructive possession of its owner and that constructive possession is sufficient to confer summary jurisdiction in the Bankruptcy Court. Collier on *Bankruptcy,* 14th ed., Vol. 2, par. 23.05, page 485. For example, see *In Re Marsters* (C.A. 7th), 101 F. 2d 365, cert. den. 306 U.S. 663, 59 S. Ct. 788, 83 L. Ed. 1059, where the asset was a judgment owned by the bankrupt; *In Re Worral* (C.A. 2d) 79 F. 2d 88 where the asset was a seat on the New York Stock Exchange; and *Benton v. Calloway* (supra) where the asset discussed in dicta was a lessor's reversion.

A lienholder not in possession of the property upon which he claims a lien is not an adverse holder and the Bankruptcy Court may determine questions as to the lien in a summary proceeding. See *Dugan v. Logan,* 229 Ky. 5, 16 S.W. 2d 763 at 766, cert. den. 280 U.S. 587, 50 S. Ct. 36, 74 L. Ed. 636; *Fish v. East* (C.A. 10th) 114 F. 2d 177 at 194. Appellants were not in possession of the real property.

Thus Mrs. Weaver's fee title to the land—her "reversion"—was intangible property in the constructive possession of the Court and the Court had the summary jurisdiction to rule on the validity of the deed of trust which could have destroyed the reversion.

**4. The Summary Jurisdiction of the Bankruptcy Court Includes the Power to Determine the Validity of a Lien Against the Debtor's Ranch.**

Section III of appellants' argument is devoted to the proposition that the Bankruptcy Court had no

jurisdiction because Ch. XI Arrangements are meant to affect only unsecured indebtedness. (Appellants' Opening Brief, pp. 20-25.) Appellants summarize their position with this amazing statement:

> "It is not a question of constructive possession either. The existence of a lien or other security automatically divests the Bankruptcy Court of jurisdiction in a Chapter II proceeding." (Appellants Opening Brief, p. 25.)

Unfortunately none of the cases cited by petitioners are in point. Generally all they do is discuss the general proposition that a plan of arrangement is meant to affect only unsecured creditors of the debtor. No one denies the correctness of that rule in context. But here the issue is whether the referee has jurisdiction to determine the validity of a lien claimed against the debtor's property. The correct rule is that valid liens existing at the time of the commencement of either a bankruptcy or Chapter XI arrangement proceeding will not be distributed, *except* that they are subject to administration in the Bankruptcy Court and the Court always has the power to determine their validity, amount and priority. The case of *City of Long Beach v. Metcalf* (C.A. 9th) 103 F. 2d 483, at 486-487, cert. den. 308 U.S. 602, 60 S. Ct. 139, 84 L. Ed. 504 summarizes the rules on summary jurisdiction. See also *In Re American Fidelity Corp. Ltd.* (D.C. S.D. Cal.) 28 F. Supp. 462.

On adjudication in bankruptcy (or filing a petition in Ch. XI) title to land belonging to the bankrupt vests in the trustee or debtor in possession and juris-

diction to determine the validity and amount of lien on land and to decree the method of liquidation is lodged in the Federal Court and cannot thereafter be taken by the state Court. *Adolph Ramish, Inc. v. Laugharn* (C.A. 9th) 86 F. 2d 686. The Supreme Court of the United States has stated these rules in *Isaacs v. Hobbs Tie & Timber Co.,* 282 U.S. 734, 51 S. Ct. 270, 75 L. Ed. 645:

> "Thus while valid liens existing at the time of the commencement of a bankruptcy proceeding are preserved, it is solely within the power of a court of bankruptcy to ascertain their validity and amount and to decree the method of their liquidation." (51 S. Ct. at 272.)
>
> . . .
>
> "The jurisdiction in bankruptcy is made exclusive in the interest of the due administration of the estate and the preservation of the rights of both secured and unsecured creditors." (51 S. Ct. 272.)

These same rules are stated by the Ninth Circuit Court of Appeals in *Heffron v. Western Loan and Building Co.,* 84 F. 2d 301:

> "While valid liens created more than four months prior to the filing of the petition are declared by section 67 of the Bankruptcy Act to be unaffected by bankruptcy proceedings, such liens nevertheless may be subjected to administration by the court and their validity and enforcement determined and carried out by the court."

Specific cases holding security interests invalid by the Bankruptcy Court are *In Re Kellogg* (C.A. 2d)

121 Fed. 333 where a mortgage upon real property was held void for usury; and *In Re Rochford* (C.A. 8th) 124 Fed. 182, where a chattel mortgage was held void as against creditors of the bankrupt. Both cases are directly in point. The issue on appeal was whether the question of validity and amount of a mortgage lien upon property of the bankrupt estate can be determined in a summary proceeding before a referee.

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## II.

**THE PETITIONER WILLIAM CLARK PURCHASED THE OVERDUE WEAVER SENIOR NOTE AND WAS THEREFORE NOT A HOLDER IN DUE COURSE AND WAS SUBJECT TO THE DEFENSES OF FRAUD, MISTAKE AND FAILURE OF CONSIDERATION UNLESS THE WEAVERS ARE ESTOPPED TO ASSERT THEM. THE REFEREE'S FINDINGS AGAINST ESTOPPEL ARE FULLY SUPPORTED BY THE EVIDENCE.**

The only attack upon the merits of the Referee's decision is made on the ground that Mrs. Weaver is estopped to attack the rights of appellant William J. Clark. (Appellant's Opening Brief, Section IV, pp. 26-27.) The estoppel defense is not urged as to appellant Pasadena Investment Co. (Appellant's Opening Brief, p. 8.) Nor is their any appeal from the Referee's fraud findings (Appellant's Opening Brief, p. 6), yet appellants entitle Section V of their opening brief, "Appellant Does Not Need to Belabor The Question Whether There Was Some Evidence of Fraud"! (pp. 28-33). Having conceded that they acquiesce in the evidentiary support for the findings

of fraud, appellant's discussion can only be presumed to be an attempt to leave this Court with the impression that somehow there was no fraud and in any event another Court should have ruled on that question.

As to the estoppel defense raised by appellant Clark, in his trial brief to the Bankruptcy Court, Mr. Clark conceded that he is not a holder in due course, having purchased the Weaver Senior note after its maturity. (California Civil Code Section 3133 (2). Therefore, Mr. Clark is subject to all of the grounds for rescission of fraud, mistake and failure of consideration which Mrs. Weaver has against Pasadena Investment Company unless Mrs. Weaver is estopped to assert them. *Pacific Southwest Trust and Savings Bank v. Valley Finance Corporation,* 99 C.A. 728 (California Supreme Court hearing denied).

By Mr. Clark's own testimony it is clear that when he purchased the Weaver note and deed of trust from Pasadena Investment Company, in February 1965, he did not depend solely upon the Weaver letter of July 23, 1964. (Debtor's Exhibit 11; R.T. p. 493, line 8 through p. 495, line 10.) Upon his demand for proof that consideration was given for the note and deed of trust, Pasadena Investment Company showed him its cancelled check to the Weavers for $51,000.00. (R.T. p. 494, lines 8 and 9 and p. 495, lines 2-7; Debtor's Exhibit 10.) That check never represented payment of money at all (R.T. p. 299, line 3 to p. 301, line 3), but Pasadena did not hesitate to represent it as the purported consideration for the Weaver Senior

note and deed of trust. Mr. Clark's testimony also shows that Pasadena falsely represented to him that no interest had been paid on the Weaver Senior note and that he was entitled to the accrued interest (R.T. p. 493, lines 14-19) which would have been $5,440.00 at the time he purchased the note. (Other evidence proved that while the Weavers had not paid any interest on their note, Pasadena Investment Company had paid itself $3,047.98 of interest from the money it controlled in the Hume Lake Cattle Company rebate account.) (R.T. p. 290, lines 17-23; p. 318, lines 3-10.) So, Mr. Clark purchased the overdue note knowing that the Weavers had never paid one penny on principal or interest (R.T. p. 493, lines 16-17) and without talking to any of the Weavers or visiting the Weaver ranch (R.T. p. 500, lines 7-15.)

It is clear from the record that Mr. Clark relied just as much on the misrepresentations of Pasadena Investment Company that they had paid the $51,000.00 cash for the Weaver Senior note and deed of trust and that there was $5,440.00 accrued interest on the note to induce him to purchase it as there was any reliance by Mr. Clark upon the Weaver Senior's signature to the letter of July 23, 1964. (R.T. p. 493, line 8 to R.T. p. 495, line 9.) It is doubtful that Mr. Clark, an attorney at law (R.T. p. 491, lines 20-21), should even be able to claim justifiable reliance on the letter of July 23, 1964 since it is not addressed to him or any other third party and was six months old at the time he took the assignment of the note and trust deed (Debtor's Exhibit 11).

There is no serious threat of harm to Mr. Clark because Pasadena Investment Company is fully willing and able to reimburse him. Pasadena Investment Company made a big point of its financial standing and the fact that it had a million eight hundred thousand dollar line of credit with the Bank of America. (R.T. p. 421, lines 5-11.) The appellants have inferred by their "Stipulation Staying Portion of Order Pending Determination, etc." (T. p. 84) that Pasadena Investment Company is ready to reimburse Mr. Clark, if, in fact, it has not already done so. If this case were to be decided upon the basis that Mrs. Weaver was estopped to assert the fraud, mistake and failure of consideration and the case were not allowed to be decided on the merits, the result would be disastrous to Mrs. Weaver and unjustly enrich Pasadena Investment Company. In that case, Pasadena Investment Company would be allowed to keep the $50,508.55 paid to it by Mr. Clark (R.T. p. 487) and Mr. Clark would take the Weaver ranch which he believes is worth at least $1,100.00 an acre, or approximately $60,500.00 (R.T. p. 492).

This obviously unjust result is not called for by the law of estoppel. First, the existence of an estoppel is a question of fact for the trier of fact in each case. (*GMAC v. Gandy,* 200 Cal. 284, 253 P. 137.) Estoppel rests upon sound equitable principles and the Courts may properly "balance the equities" in determining whether an estoppel is established. (*Smith v. Rasqui,* 176 C.A. 2d 514 at 519, 1 Cal. Rptr. 478.) Estoppel is a harsh remedy because it prevents a decision on the

merits. Therefore, it is never applied except where to allow the truth would be to consummate a wrong to one party:

> ". . . 'The law does not favor estoppels, for their effect is to prevent the party against whom they are invoked from proving the truth of the matter, to ascertain which, as a general proposition, is the great end of judicial inquiry. . . The doctrine is a harsh one, and is never to be applied except where to allow the truth to be told would consummate a wrong to the one party or enable the other to secure an unfair advantage.'(*Franklin v. Merida,* 35 Cal. 558, 566 . . .; *Wheaton v. Insurance Company,* 76 Cal. 416, 430.)" (*Fair Oaks Bank v. Johnson,* 198 Cal. 196, at 202, 244 P. 335.)

The required elements of estoppel are clear and each one must be present or there can be no estoppel.

> "In order to constitute an equitable estoppel, estoppel by conduct, or estoppel in pais there must exist a false representation or concealment of material facts; it must have been made with knowledge, actual or constructive, of the facts; the party to whom it was made must have been without knowledge or the means of knowledge of the real facts; it must have been made with the intention that it should be acted upon; and the party to whom it was made must have relied on or acted on it to his prejudice." 31 C.J.S. Estoppel §67.

The same elements are recognized in both California and Federal cases. See *Hampton v. Paramount Pictures Corp.* (C.A. 9th) 279 F. 2d 100 at 104, cert. den.

364 U.S. 882, 81 S. Ct. 170, 5 L. Ed. 103; *California Cigarette Concessions, Inc. v. City of Los Angeles,* 53 C. 2d 865 at 869, 3 Cal. Rptr. 675, 350 P. 2d 715.

The burden of proving each element of equitable estoppel is upon Mr. Clark, the party asserting the defense and each element must be proved by clear, convincing and satisfactory evidence. *Cedar Creek Oil & Gas Co. v. Fidelity Gas Co.* (C.A. 9th) 249 F. 2d 277 at 281, cert. den. 356 U.S. 932, 78 S. Ct. 775, 2 L. Ed. 763.

If any one of the required elements is missing there can be no estoppel. *Riley v. Brown,* 72 C.A. 468 at 478, 237 P. 833.

The Referee's findings which relate to the estoppel issue are fully supported by the evidence:

> "On July 23, 1964, petitioner and her husband signed a letter (Ex. 11) at the request of Pasadena Investment Co. (R.T. p. 441, line 11 to p. 442, line 17) stating that they had no counter claims or disputes to their promissory note. Pasadena Investment Co. made no further disclosures to the Weaver Seniors. (R.T. p. 447, line 22 to p. 449, line 9.) Petitioner's husband, Charles L. Weaver, Sr. died on August 18, 1964 (Debtor's Ex. 2; R.T. p. 19, lines 8-9); leaving all of his property to petitioner. He never knew of the fraud of Pasadena Investment Co. nor of the facts found above to constitute grounds for rescission based upon mistake and failure of consideration. (R.T. p. 441, line 11 to p. 442, line 17; R.T. p. 97, lines 1-11; R.T. p. 98, line 15 to p. 101, line 22; R.T. p. 230, lines 16-21.) Neither

is he chargeable with such knowledge, constructively or otherwise. Petitioner did not know of the fraud of Pasadena Investment Co. nor of the facts constituting grounds for rescission based upon mistake and failure of consideration (R.T. p. 441, line 11 to p. 442, line 17; R.T. p. 97, lines 1-11; R.T. p. 98, line 15 to p. 101, line 22; R.T. p. 230, lines 16-21) until an investigation commenced by her attorneys at the time notice of default under the trust deed was given. (R.T. p. 101, lines 9-22.) Petitioner is not chargeable with such knowledge prior thereto, either constructively, or otherwise. . . ." (Findings of Fact, Paragraph IV, T. p. 57; References to Reporter's Transcript added.)

". . . The respondent, William J. Clark, purchased the Weaver, Sr. note and trust deed from Pasadena Investment Co., without recourse, for valuable consideration after the note was mature and the extension of its due date had expired. (Debtor's Exs. 50, 8 and 9; R.T. p. 487, lines 6-8.) Clark had had past business dealings with Pasadena Investment Co. (R.T. p. 487, lines 24-25.) In the negotiations leading to his purchase of the subject past-due note and trust deed, Pasadena Investment Co. showed Clark the note and trust deed, the letter of July 23, 1964 (Ex. 11), and its cancelled check for $51,000.00 to the Weavers (Ex. 10). (R.T. p. 493, line 20 to p. 495, line 10.) Pasadena Investment Co. falsely represented to Clark that Pasadena's check for $51,000.00 was the consideration paid by it for the Weaver Senior's $51,000.00 note and deed of trust. (R.T. p. 495, lines 2-10; R.T. p. 299, line 3 to p. 301, line 3; R.T. p. 474, line 2 to p. 475, line 6.) It

also falsely represented to him that no interest had been paid on the note so that he would be entitled to 16 months of accrued interest in the sum of approximately $5,440.00 when, in fact $3,047.98 of interest on this note had been paid to Pasadena Investment Company from Hume Lake Cattle Co. (R.T. p. 493, lines 15-19; R.T. p. 290, lines 17-19.) Clark made no inquiry to the makers of the note, or any of them, before purchasing it but relied on the representations made by Pasadena. (R.T. p. 500, lines 4-17; R.T. p. 493, line 8 to p. 495, line 10.) Pasadena Investment Company is financially solvent and capable of making full restitution to Mr. Clark with whom it has had friendly business relations in the past. (R.T. p. 301, lines 14-20; R.T. p. 421, lines 5-11.) The respondent Clark, having purchased the Weaver Senior note and deed of trust subject to existing personal defenses of the makers against Pasadena Investment Company, under these facts, the court finds that Clark is not entitled to assert equitable estoppel against petitioner." (Findings of Fact, Paragraph V, T. p. 57; References to Reporter's Transcript added.)

Several of the required elements of equitable estoppel are missing in this case. First, when Mr. and Mrs. Weaver, Sr. signed the letter of July 23, 1964 (Debtor's Exhibit 11) stating that in consideration for an extension of the due date of the note "We hereby reaffirm that the amount and terms of said note are correctly stated and that there will be no counter claims or disputes", they were without knowledge, actual or constructive, that the consideration for their note and trust deed was not a loan

of $51,000.00 as had been represented to them by Pasadena Investment Company. They had no knowledge that in fact Pasadena Investment Company had taken back its check for $51,000.00 and that no money had passed on August 28, 1963 and that they had grounds to rescind their note and trust deed for fraud, mistake and failure of consideration. (Findings of Fact, Par. IV, T. p. 57.) Without knowledge of the grounds for rescission, Mrs. Weaver cannot be estopped. See *Hampton v. Paramount Pictures Corp.* (C.A. 9th) 279 F. 2d 100 at 104, cert. den. 364 U.S. 882, 81 S. Ct. 170, 5 L. Ed. 103; *California Cirgaette Concessions, Inc. v. City of Los Angeles,* 53 C. 2d 865 at 869, 3 Cal. Rptr. 675, 350 P. 2d 715.

Second, the "representations" relied upon by Mr. Clark to create an estoppel were not made to Mr. Clark and were not made with the intention that they should be acted upon by any third party. Recall that the statements by the Weavers were in the form of a postscript to a letter from Pasadena Investment Company to them concerning an extension of the due date of the note. Nowhere does it purport to be addressed to Mr. Clark or generally to any third party potential assignee of the note. Contrast this with the facts of *Kelly v. Universal Oil Supply Co.,* 65 Cal. App. 493, 224 P. 261, cited by appellants. The plaintiffs in that case had issued their promissory note with the understanding that it would be negotiated to secure money to start drilling operations under an oil lease which the maker of the note could cancel if drilling operations were not started within a certain period of

time. To further the negotiation of their promissory note, the plaintiffs delivered to the payee of the note a letter addressed to Pacific Mortgage Company dated December 5, 1920 which recited the particulars of making the note, the fact that it was secured, etc. and stated as follows.

> "That I have no offsets, claims nor defense against said note except as stated above. I understand that it (is) desired to assign said note and mortgage." (65 Cal. App. at 496.)

This written statement signed by both plaintiffs was made with the expectation that the payee would exhibit it to any person interested in buying the note and he did so on December 8, 1920 receiving $4,600.00 in cash from one Hamil who then on December 14, 1920 assigned the note to the Glendale National Bank nine days from the date the letter was written. Since there were no conditions attached to the note, the bank did not know that it could be cancelled under the agreement between plaintiffs and the payee if drilling operations were not commenced.

By contrast, in our case the Weavers did not know of the grounds for rescission at the time the letter of July 23, 1964 was signed; they did not sign the letter addressed to potential assignees or with the intent that it be exhibited to any third parties, and the letter they did sign was six months old when Mr. Clark asserts that he relied upon it.

## CONCLUSION

The petition of Marguerite J. Weaver to determine the validity of any claims of lien by William J. Clark, Pasadena Investment Company or Title Insurance and Trust Company was fully tried and extensively argued and briefed before Referee Franson before his decision. The presentation of evidence took three very full trial days and the evidence was fully developed. The trial was "summary" only in the limited sense that the term has historically been used to designate the jurisdiction of the Bankruptcy Court to hear and to determine claims against the property owned by the debtor or bankrupt. The Referee, as trier of fact, had full opportunity to observe the manner and demeanor of witnesses and form conclusions concerning their credibility. His findings of fact are fully supported by the evidence and the Referee's Order is fully supported by the law.

Wherefore, Marguerite J. Weaver, as debtor in possession, prays that the District Court's Order affirming the Order of the Bankruptcy Court be affirmed.

Dated, Fresno, California,
November 21, 1966.

Respectfully submitted,

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CERTIFICATE OF COUNSEL

I certify that, in connection with the preparation of this brief, I have examined Rules 18 and 19 of the United States Court of Appeals for the Ninth Circuit, and that, in my opinion, the foregoing brief is in full compliance with those rules.

RICHARD W. DIETRICH,
*Attorney for Appellee.*